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SUBJECT: GCC EQUITIES: INVESTMENTS OR LOTTERY TICKETS?

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¶1. (SBU) Summary. During a meeting with the Ambassador October 26, National Bank of Kuwait (NBK) CEO said skyrocketing GCC equities could presage a Gulf equivalent of the U.S. "dot com" market bust. In order to "shake up the market a bit," NBK will host a December 18 symposium to examine the economic integrity of GCC equity trades. Citing the Central Bank Governor as the only "responsible" economic voice today in Kuwait, NBK officials expressed concern that there is "a risk of the bubble bursting" due to market instability. End Summary.

¶2. (U) On October 26, Ambassador met at the National Bank of Kuwait (NBK) with CEO Ibrahim Dabdoub (at his invitation) and the bank's Senior Economist, Ms. Randa Azar-Khoury, regarding the December 18 "NBK Symposium on GCC Equity Markets: Fundamentals-Driven Markets or Asset Bubbles?" Dabdoub and Azar-Khoury expressed NBK concern over the unprecedented "stellar performance" and volatility of the region's equity markets over the past three years.

¶3. (U) The NBK officials noted that improved economic fundamentals and a market-friendly post-Iraq War political environment initiated the growth. Nevertheless, they said, they are convening the symposium for regional experts to examine whether the growth represents a sustainable trend or is simply more excess liquidity pursuing fewer real assets. As Dabdoub put it, "It's like a blood pressure of 200 over 100, very high, very much like the 'dot com' bubble in the States."

4) (U) Azar-Khoury laid out some statistics. For example, the regional price-to-earnings ratios that normally run in the low teens have soared to multiples of 40 and 50 times in the UAE and Qatar. Moreover, in a region that traditionally has prized cash dividends, current yields have sunk to the 1 percent range. A "sizable part of Kuwaiti bank loan portfolios is being used to finance equity trades; there is a risk of the bubble bursting," she said.

5) (SBU) Dabdoub, noting that NBK's board is "quite conservative," cautioned, "We are worried about a crash." He said that the only "responsible" economic policy voice in the Kuwait government today is that of Central Bank Governor, Sheikh Salem Saud AbdulAziz Al-Sabah. "The rest speak rubbish; they are afraid of being seen as Cassandra these days," he said. Dabdoud continued that the symposium was designed to "shake people up a little." He used a metaphor

as the rationale for the symposium, "It's better to fall from the second floor and break a leg than from the third floor and break your neck!" He said that today "we are at 200 percent GDP in the market and 860 times the net cash flow for companies purchased in the market." "Saudi Arabia is even worse," he cautioned.

6) (U) Azar-Khoury pointed out that the Central Bank Governor had "imposed a global loan to deposit ratio of 80 percent," and that this had helped slow down the rate of credit growth. Nevertheless, she complained, the government's "wanting people to be happy in the good times," placed the financial system at risk needlessly, especially so in this time of high petroleum prices.

7) (SBU) Azar-Khoury found it "alarming" that the ratio of market capitalization to private sector GDP was more than 800 percent and that the market capitalization in September was 200 percent of Kuwait's GDP in 2004. Ambassador agreed that the situation was volatile and noted that countries often are judged as much on their fiscal responsibility in good times as in bad times. For example, he mused, how might Kuwait get a functioning tax system in place during a time of unprecedented, oil-generated surpluses? It was, he remarked, "a wealth management exercise," with no easy solution. He applauded the GOK's determination to withstand pressure from some in the National Assembly to use budget surpluses to pay off citizens' private debts.

LEBARON